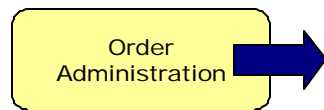


Executive Summary: Overall Control Evaluation and Key Management Issues

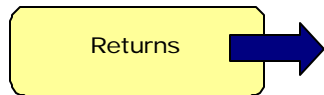
Overall Control Evaluation:

Overall, key controls governing the order administration, RMA, inventory control, T&E, payroll and accounts payable processes at GIJ are adequate and operating on a consistent basis. However, opportunities for control and efficiency improvements are highlighted below. Details can be found in the Action Matrix section of each process.

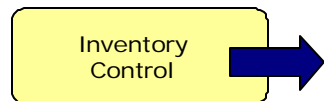
Key Management Issues:



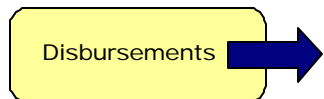
- Purchase orders are not reviewed by sales management until they are already entered into Oracle (*Action Matrix #1*)
- Although all required information is available in Oracle, sales orders are tracked manually using Excel spreadsheets. (*Action Matrix #2*)
- Order processing statistics are not generated on a regular basis to measure and evaluate effectiveness and efficiency. (*Action Matrix #3*)



- RMA processing is inefficient and does not fully utilize Oracle. (*Action Matrix #5*)
- The RMA approval/creation process results in decreased swap-stock controls and non-standard cycle time measurements. (*Action Matrix #6*)
- RMA processing requires manual tracking. Because there is no reconciliation of all RMA-related shipments and receipts, management cannot monitor RMA volume and activity. (*Action Matrix #7*)



- Procedures to verify that all scheduled shipments have been both shipped and shipped to the proper location are limited. (*Action Matrix #11*)



- There is inadequate segregation of duties in the current wire transfer system; mitigating controls should be strengthened. (*Action Matrix #13*)



Executive Summary: Objectives, Scope and Work Performed

Objectives

- ❖ Determine GIJ compliance with relevant corporate and local policies and procedures.
- ❖ Evaluate overall efficiency and effectiveness of internal controls and procedures for each of the processes reviewed.
- ❖ Identify opportunities for improvement in operational efficiencies and management reporting.

Scope and Work Performed

	① Process Interviews	② Detail Testing and/or Documentation Review	③ Analyze Data	④ Comparison to “Best Practices”
Order Administration *	●	●	●	●
RMA Processing	●	●	●	●
Inventory Control	●	●	●	●
Travel & Entertainment **	●	●	●	●
Payroll**	●	●	●	●
Purchasing & A/P**	●	●	●	●

* Order Administration review includes sales order entry, credit control, credit memo entry and invoicing.

** Per management’s request, we performed high level reviews of these processes with slightly more focus on travel and entertainment and payroll than on purchasing and A/P

- ① Interviews of management and key process personnel to obtain an understanding of process operation, controls and key issues. Validation of management statements as deemed necessary.
- ② Review of policies and procedures and other relevant supporting documents. Detail testing of sample transactions to confirm operation of key controls.
- ③ Analysis of database information to assess process performance.
- ④ Comparison of Generic’s practices with “Best Practices” and key internal control practices.



Internal Controls and Best Practices Assessment

The following pages display scorecards with ratings for internal controls and Best Practices. The Action Matrix following these pages describes the detail issues related to ratings which are not adequate.



Order Administration: Internal Control Assessment & Best Practices

Internal Control	Rating	Action Matrix Ref.
Management has developed clear guidelines on how the process is to function. Procedures are well documented, easily accessible and adequately maintained.	●	
Management receives accurate and relevant information.	●	
Transactions are authorized by appropriate personnel, with adequate segregation of duties.	▲	4
Transactions are based on valid sales and return transactions.	●	
Transactions are accurately processed based on information obtained by sales agents and customers.	●	
The process captures all sales. The products shipped are based on valid sales orders.	●	
The proper process is followed for the entirety of the transaction.	▲	1
Transactions are processed in a timely and efficient manner.	●	

● **Adequate:** *Control exists and is operational.*

▲ **Improvement Needed:** *Moderate risk exists due to a missing or inadequate control.*

■ **Critical:** *Significant risk exists due to a missing or inadequate control.*

Best Practice

One primary contact point is provided for each type of customer.	●	
A simple, easy to use order taking process is in place.	●	
An integrated system that is informative, flexible, and used throughout the company exists for processing and monitoring orders.	▲	2
Decisions are made at the time of customer contact.	●	
Order processing activity is measured with appropriate performance metrics, such as cycle time and fill rates. Achieved performance levels are monitored and tracked in comparison with established goals.	■	3

● **Good:** *Use of "Best Practice" is adequate*

▲ **Moderate Use:** *Improvement possible in order to achieve "Best Practice" status.*

■ **Limited/Some Use:** *Improvement recommended to improve process efficiency/effectiveness.*



RMA: Internal Control Assessment & Best Practices

Internal Control	Rating	Action Matrix Ref.
Management has developed clear guidelines on how the process is to function. Procedures are well documented, easily accessible and adequately maintained.	▲	9
Returns are properly authorized and accurately recorded.	●	
Transactions are authorized by appropriate personnel, with adequate segregation of duties.	●	
Transactions are based on valid return transactions.	▲	6
Management receives accurate and relevant information regarding RMA processing.	▲	6, 7
Performance measures to control and improve the process are utilized, adequate, and reliable.	▲	6

● **Adequate:** Control exists and is operational.

▲ **Improvement Needed:** Moderate risk exists due to a missing or inadequate control.

■ **Critical:** Significant risk exists due to a missing or inadequate control.

Best Practice

Appropriate measurement, tracking, and reporting systems are designed to allow monitoring of RMA management and resolution on an ongoing basis.	▲	7
Current technology is used to facilitate sales return and replacement processing, such as current Oracle functionality, web-based customer service or EDI functionality.	■	5
Key performance indicators are used to continuously improve RMA handling and eliminate the underlying causes if possible.	▲	8
Sales Return personnel are continually trained on most effective and efficient procedures to improve the way customer RMAs are processed.	●	

● **Good:** Use of "Best Practice" is adequate

▲ **Moderate Use:** Improvement possible in order to achieve "Best Practice" status.

■ **Limited/Some Use:** Improvement recommended to improve process efficiency/effectiveness.

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Inventory Control: Internal Control Assessment & Best Practices

Internal Control	Rating	Action Matrix Ref.
Inventory receipts and shipments are properly authorized, accurately recorded and validated.	▲	10
All transactions are authorized by appropriate personnel.	●	
Transactions are based on valid pick tickets.	●	
Management receives accurate and relevant information regarding inventory status and movements.	●	
Inventories are physically safeguarded to prevent damage and loss.	●	
Policies and procedures are documented and communicated to ensure all personnel understand objectives and responsibilities.	●	

● **Adequate:** Control exists and is operational.

▲ **Improvement Needed:** Moderate risk exists due to a missing or inadequate control.

■ **Critical:** Significant risk exists due to a missing or inadequate control.

Best Practice

Criteria are established to serve as a basis for selecting performance indicators relevant to management and warehouse personnel.	●	
Use historical and predictive forecasting techniques to assess future inventory needs.	●	
Warehousing function is used as a key customer service weapon, and warehousing strategy focuses on meeting and exceeding customer expectations.	●	
Inventory balances are adequately evaluated.	▲	10, 12

● **Good:** Use of "Best Practice" is adequate

▲ **Moderate Use:** Improvement possible in order to achieve "Best Practice" status.

■ **Limited/Some Use:** Improvement recommended to improve process efficiency/effectiveness.



Action Matrix

The following matrix displays our detailed observations and recommendations. Management's action plan (jointly developed by Arthur Andersen and Generic Inc. Japan), is described, along with the responsible party. In addition, observations have been given a priority ranking of high, medium, or low representing the degree of control risk or opportunity for process improvement.



Action Matrix

	Issue/Observation	Management Implementation Plan	Process	Responsible Party	Priority/Timing
1	<p>Issue: Customer purchase orders are consistently entered into Oracle and then reviewed by sales management after the fact.</p> <p>Business Impact: Sales orders may be inappropriately created.</p>	<p>A) Ensure that customer purchase orders are reviewed and approved by sales management before they are processed by sales administration. Purchase orders should be reviewed after processing only in exceptional cases.</p>	<p>Order Administration</p>	<p>Sales Administration: John Smith</p>	<p>High Feb 1999</p>
2	<p>Issue: Sales order tracking involves manually updating Excel spreadsheets. Although all the information in the spreadsheets exists in Oracle, the spreadsheets are used because they combine information from two separate Oracle reports in one spreadsheet.</p> <p>Business Impact: Utilization of manually created spreadsheets increases the risk of errors resulting in inaccurate monitoring, analysis and business decisions.</p>	<p>A) Seek IS assistance in investigating how the Oracle Backlog and Billing reports can be altered or seek training as to how to efficiently export and merge the Oracle report information in Excel.</p>	<p>Order Administration</p>	<p>Sales Administration: John Smith</p>	<p>Medium May 1999</p>



Action Matrix

	Issue/Observation	Management Implementation Plan	Process	Responsible Party	Priority/Timing
3	<p>Issue: There are currently no performance measurements related to order administration, such as:</p> <ul style="list-style-type: none">• cycle times• level of activity/volume• new orders vs. re-orders• statistics by customer• accuracy rates <p>Business Impact: Without evaluating internal processes, GIJ can not effectively change and improve procedures and workflow related to order fulfillment.</p>	<p>A) Work with Corporate and other regions to determine key performance measurements related to the order administration process and utilize technology (i.e., SAP, Oracle, Excel) to extract such measurements.</p>	<p>Order Administration</p>	<p>Sales Administration: John Smith</p>	<p>Medium April 999</p>
4	<p>Issue: Sales Administration personnel have Oracle system access to the sales and inventory modules and physical access to the sample drive inventory.</p> <p>Business Impact: The ability of personnel to access Oracle, issue a credit memo and obtain physical drives increases the risk that theft of these drives could occur undetected.</p>	<p>A) Controls governing the tracking and physical security of sample drives should be strengthened as follows:</p> <ul style="list-style-type: none">• Finance should agree invoices/credit memos to shipping and other supporting documentation from sales administration to ensure that transactions are valid.• The custody of the key to sample drives should be designated to an independent party	<p>Order Administration</p>	<p>Sales Administration: John Smith</p>	<p>Low March 1999</p>



Action Matrix

	Issue/Observation	Management Implementation Plan	Process	Responsible Party	Priority/Timing
5	<p>Issue: As a service to Japan customers, GIJ handles all shipments of defective drives to the Customer Service Center (CSC) and repaired drives to customers. This activity could typically, under standard GIJ procedures, be handled between the customer and CSC only. Consequently, Oracle cannot be used for much of the activity.</p> <p>Business Impact: RMA processing is inefficient and not cost-effective as it requires resources to process transactions that can be done directly between the customer and CSC.</p>	<p>A) <i>To eliminate GIJ's physical handling of RMA drives, the swap-stock warehouse will be outsourced to a forwarder effective April 1, 1999. The forwarder will handle shipments to CSC and the local customers.</i></p>	RMA	Sales Administration: John Smith	High April 1999
6	<p>Issue: The RMA approval process involves RMA creation only at the point of receipt of the defective drives rather than the point of customer request. This has resulted in the following:</p> <ul style="list-style-type: none"> • Cycle time measurements and open RMA tracking differ from the WD standard. • Oracle cannot be used to trigger and record swap-stock movement. Thus, Sales Administration must manually initiate swap drive shipments. However, there are no procedures at the back-end (i.e., warehouse) to ensure the sales administration does so only after receipt of defective drives. <p>Business Impact: The current RMA approval process prevents proper performance measurements and reduces swap-stock handling efficiency and controls.</p>	<p><i>GIJ is working with Corporate to determine the details and timing of a new system that adequately and properly captures all RMA's.</i></p> <p><i>Until the new system is initiated, warehouse staff will validate the swap drive pick list provided by Sales Administration against the original RMA application, which provides details of the received defective drives.</i></p>	RMAs	Sales Administration: John Smith	High March 1999

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Action Matrix

	Issue/Observation	Management Implementation Plan	Process	Responsible Party	Priority/Timing
7	<p>Issue: Because GIJ's RMA process differs from standard GI procedures, Oracle cannot accommodate all the RMA activity. Therefore, primarily manual methods must be used to receive, ship and track RMA activity. There are currently no procedures to measure receipt and shipment volumes and to ensure, on a control total basis, that RMAs are being properly processed.</p> <p>Business Impact: Inadequate reconciliation procedures prevents management from effectively monitoring RMA activity .</p>	<p>A) From now through April 1999, sales administration management will implement procedures to review and monitor, on a control total basis, receipt and shipment information for both swap RMAs and repair RMAs.</p> <p>B) GIJ will ensure that, once the warehouse is outsourced, tracking and monitoring continues either through the forwarder's system or through a procedure similar to A) above.</p>	RMAs	Sales Administration: John Smith	High March 1999
8	<p>Issue: There is no mechanism to track and monitor reasons for RMA activity.</p> <p>Business Impact: Lack of a tracking mechanism prevents management from improving processes to reduce RMA activity and increasing customer satisfaction.</p>	<p>A) GIJ will develop reason codes based on the listing developed by Corporate and establish a mechanism to track, monitor and report results.</p>	RMA	Sales Administration: John Smith	Medium April 1999



Action Matrix

	Issue/Observation	Management Implementation Plan	Process	Responsible Party	Priority/Timing
9	<p>Issue: Current documentation of policies, procedures, and work instructions pertaining to RMA tracking and warehouse activity is limited.</p> <p>Business Impact: A lack of complete, documented, and updated policies and procedures could result in processing errors and irregularities, increase training costs, and reduce employee productivity during employee transition.</p>	A) Document general and specific work instructions and distribute to management and warehouse personnel.	RMA	Sales Administration: John Smith	Low April 1999
10	<p>Issue: Although inventory aging is informally and periodically performed by Finance, this function is not formally performed by Sales Administration, who controls the swap-stock and sample inventory.</p> <p>Business Impact: Inadequate inventory aging analysis prevents GIJ from determining:</p> <ul style="list-style-type: none">a) when/how to decrease/increase inventory levels andb) the effectiveness of forecasting for swap-stock and sample drives	A) Sales administration will seek assistance from Corporate and IS to create a custom report or determine existence of an Oracle report that shows inventory receipt dates.	Inventory Control	Sales Administration: John Smith	Medium May 1999



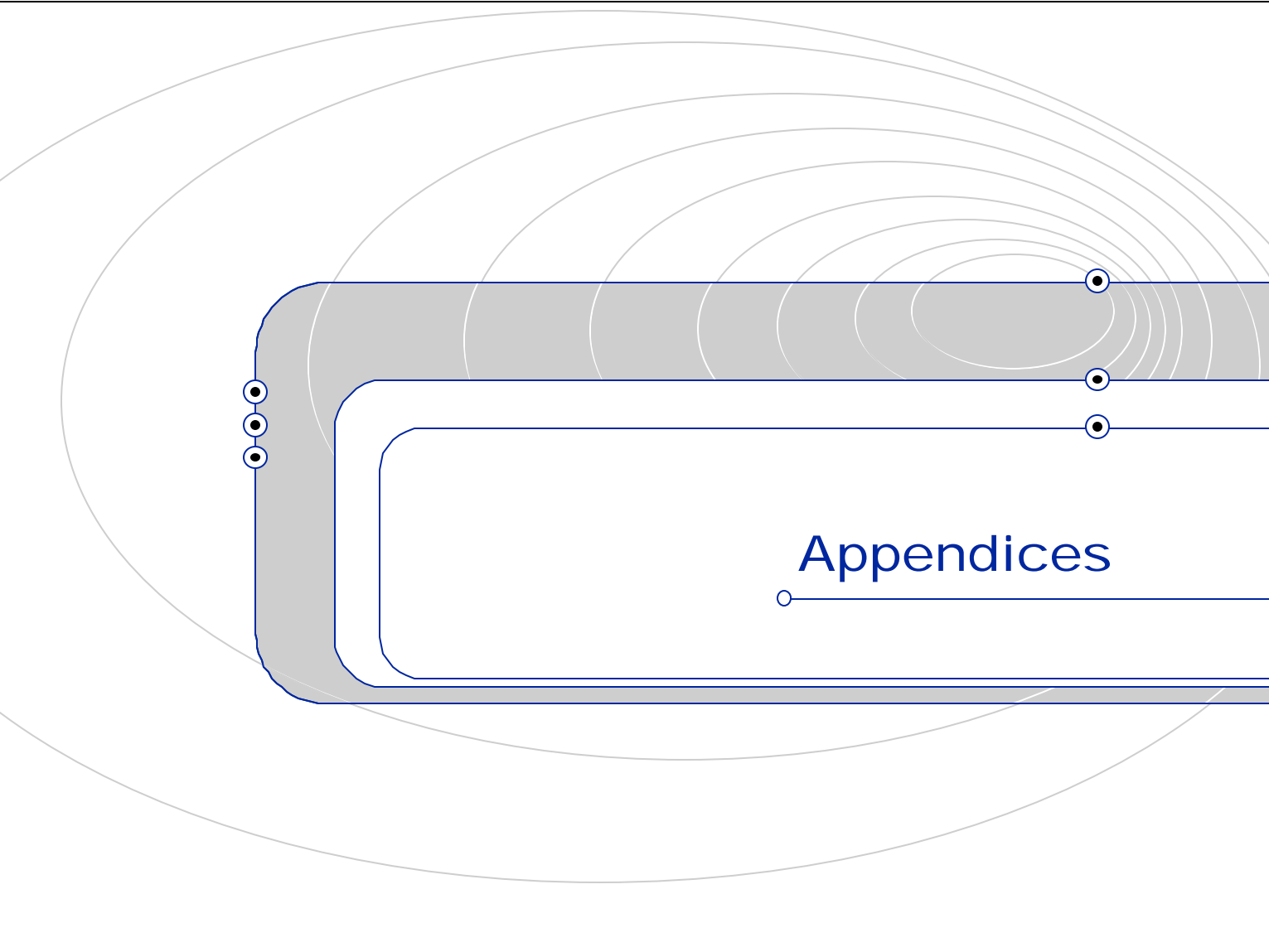
Action Matrix

	Issue/Observation	Management Implementation Plan	Process	Responsible Party	Priority/Timing
11	<p>Issue: Procedures to verify that all scheduled shipments have been both shipped and shipped to the proper location are limited. Currently, there is only one warehouse staffperson who handles shipping documents. Additionally, the same individual confirms to sales administration that all shipments based on the pick lists have been made.</p> <p>Business Impact: Inadequate procedures to verify shipments increases the risk that improper or incomplete shipments will not be detected in a timely manner.</p>	<p>A) A dual sign-off procedure that involves a second staffperson to verify shipments will be established in the office warehouse (sample drive inventory).</p>	<p>Inventory Control</p>	<p>Sales Administration: John Smith</p>	<p>Medium March 1999</p>
12	<p>Issue: Blind counts are not used during the bi-monthly physical count. The current process entails the warehouse staff first obtaining the Oracle Subinventory Report and then conducting the count.</p> <p>Business Impact: Prior knowledge of the inventory balance increases the risk that the physical count results provided differs from the true physical balance.</p>	<p>A) Implement blind count procedures whereby the warehouse staff conduct the count without Oracle balances and submit the results to Account Management, who reconciles the count to the Oracle Subinventory Report</p>	<p>Inventory Control</p>	<p>Sales Administration: John Smith</p>	<p>Low Feb 1999</p>



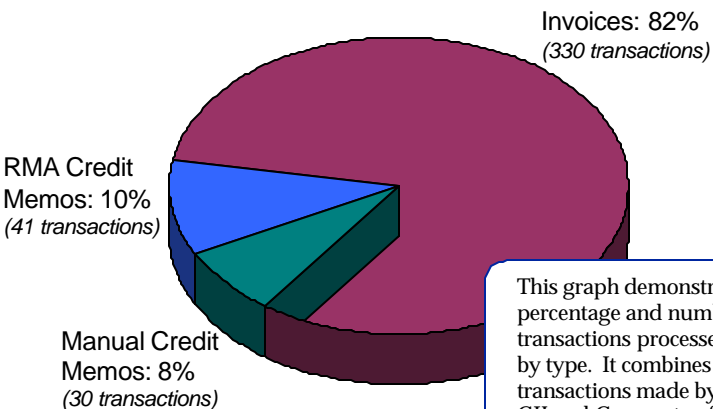
Action Matrix

	Issue/Observation	Management Implementation Plan	Process	Responsible Party	Priority/Timing
13	<p>Issue: Although disbursement duties are segregated between the accounting manager and accounting assistant, the current wire transfer system <u>allows</u> the accounting manager to open the system, enter disbursement amounts, set-up the vendor, and finally transmit payments to the bank. The accounting manager also reviews the bank reconciliations prepared by the accounting assistant. The Finance director only periodically reviews the wire transfer amount against Oracle and the supporting documentation.</p> <p>Business Impact: Inadequate controls increases the risk that unauthorized disbursements are not detected in a timely manner.</p>	<p>A) The Finance director will review disbursement amounts immediately after transmission to the bank. GJJ will also discuss with their bank the feasibility of increasing the wire transfer system controls.</p>	Disbursements	Finance: John Smith	High Feb 1999
14	<p>Issue: There are no documented work instructions (i.e., authorization procedures, management review/audit procedures, detailed payment procedures, etc.) for the payroll and disbursements functions.</p> <p>Business Impact: A lack of complete, documented and updated work instructions could result in processing errors and irregularities, increase training costs and reduce employee productivity during employee transition.</p>	<p>A) Document general and specific work instructions and distribute to finance personnel.</p>	Disbursements Payroll	Finance: John Smith	Low April 1999



Appendices

Background Information



This graph demonstrates the percentage and number of transactions processed at GIJ by type. It combines transactions made by both the GIJ and Corporate offices.

Breakdown of GIJ Transactions

Oct 98 - Dec 98

Breakdown of Invoice Activity

Oct 98 - Dec 98

This graph shows the percentage of invoice activity by customer type: OEM, OEM JIT and Distribution.

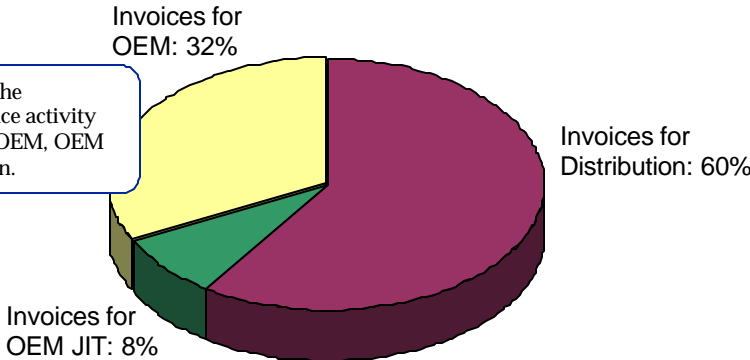






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